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A BILL FOR AN ACT

RELATING TO GENERAL EXCISE TAX EXEMPTION FOR CERTAIN SCIENTIFIC  
CONTRACTS WITH THE UNITED STATES.

**BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:**

1           SECTION 1. The general excise tax exemption for scientific  
2 contracts with the United States was intended to allow local  
3 contractors to compete with out-of-state entities for scientific  
4 contracts with federal facilities. However, today over ninety-  
5 eight per cent of these contracts are held by out-of-state  
6 entities, who pay no tax pursuant to this provision. These  
7 contracts are often large, in excess of \$800,000,000, and the  
8 annual tax loss is conservatively estimated to be between  
9 \$20,000,000 to \$40,000,000 per year. Further, the exemption has  
10 created a large administrative burden for the department of  
11 taxation, resulting in ten per cent of audit staff being used to  
12 evaluate claims for this exemption. By amending the exemption  
13 to mirror section 41 of the Internal Revenue Code,  
14 administration of the exemption will become more efficient.

15           SECTION 2. Section 237-26, Hawaii Revised Statutes, is  
16 amended to read as follows:

1           "§237-26 Exemption of certain scientific contracts with  
2 the United States. (a) Any provision of law to the contrary  
3 notwithstanding, there shall be exempted from the measure of the  
4 taxes imposed by chapter 237, [~~all of the~~] gross proceeds  
5 [~~derived by a contractor or subcontractor arising from the~~  
6 ~~performance of any scientific work as defined in subsection (b),~~  
7 ~~under a contract or subcontract entered into with the United~~  
8 ~~States (including any agency or instrumentality thereof but not~~  
9 ~~including national banks), and all of the gross proceeds derived~~  
10 ~~from the sale of tangible personal property by a seller of such~~  
11 ~~tangible personal property to such contractor or subcontractor;~~  
12 ~~provided the exemption herein shall apply only to such tangible~~  
13 ~~personal property which is to be affixed to, or to become a~~  
14 ~~physical, integral part of the scientific facility, or which is~~  
15 ~~to be entirely consumed during the performance of the service~~  
16 ~~required by the contract or subcontract.] received under a  
17 contract or subcontract entered into with the United States  
18 (including any agency or instrumentality thereof but not  
19 including national banks) in an amount equal to qualified  
20 research expenses for the taxable year over the base amount,  
21 basic research payments determined under Internal Revenue Code  
22 section 41(e)(1)(A), and amounts paid or incurred by the  
23 taxpayer in carrying on any trade or business of the taxpayer~~

1 during the taxable year (including as contributions) to an  
2 energy research consortium for energy research. Gross proceeds  
3 exempted under this section shall not exceed the amount properly  
4 claimed and allowable under section 41 of the Internal Revenue  
5 Code for the same taxable period.

6 (b) For purposes of this section, [~~"scientific work" is~~  
7 ~~work involving primarily the research and development for, or~~  
8 ~~the design, manufacture, instrumentation, installation,~~  
9 ~~maintenance, or operation of aerospace, agricultural,~~  
10 ~~astronomical, biomedical, electronic, geophysical,~~  
11 ~~oceanographic, test range, or other scientific facilities.~~  
12 ~~Maintenance or operation, for purposes of this section, shall~~  
13 ~~include housekeeping functions in providing certain~~  
14 ~~nonscientific logistic and support services.] "qualified  
15 research expenses for the taxable year over the base amount,"  
16 "basic research payments determined under Internal Revenue Code  
17 section 41(e)(1)(A)," and "amounts paid or incurred by the  
18 taxpayer in carrying on any trade or business of the taxpayer  
19 during the taxable year (including as contributions) to an  
20 energy research consortium for energy research" shall have the  
21 same meaning as under section 41 of Internal Revenue Code and  
22 its judicial and administrative interpretations.~~

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1 SECTION 3. Statutory material to be repealed is bracketed  
2 and stricken. New statutory material is underscored.

3 SECTION 4. This Act, upon its approval, shall take effect  
4 for taxable ears beginning after December 31, 2013.

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INTRODUCED BY:



BY REQUEST

JAN 22 2013

H.B. NO. 964

**Report Title:**

General Excise Tax Exemption for Certain Scientific Contracts  
With the United States

**Description:**

Amends general excise tax exemption for scientific contracts.

*The summary description of legislation appearing on this page is for informational purposes only and is not legislation or evidence of legislative intent.*

HB 964

JUSTIFICATION SHEET

DEPARTMENT: Taxation

TITLE: A BILL FOR AN ACT RELATING TO GENERAL EXCISE TAX EXEMPTION FOR CERTAIN SCIENTIFIC CONTRACTS WITH THE UNITED STATES.

PURPOSE: Amend the General Excise Tax exemption for certain scientific contracts with the United States.

MEANS: Amend section 237-26, Hawaii Revised Statutes.

JUSTIFICATION: When originally adopted in 1965, the intent of the scientific contracts exemption was to allow local contractors to compete with out-of-state contractors in bidding for scientific contracts with federal facilities. The exemption provided local contractors an even playing field as out-of-state contractors did not pay the GET.

Today 98 percent of all federal contracts are held by out-of-state companies and the companies pay no tax pursuant to this exemption. Moreover, this exemption uses up approximately one-third of our audit resources to resolve these issues.

The Department also believes that more taxpayers may be seeking to use this exemption due to the loss of the federal research and development tax credit in 2011.

There is insufficient data to estimate the actual revenue loss; however, based on data requested of taxpayers pursuant to Act 105 Session Laws of Hawaii 2011, revenue loss could be a minimum of \$20,000,000. This exemption has outlived its original intent and usefulness.

Impact on the public: Since all of the taxpayers who compete for scientific

contracts will be subject to General Excise Tax, the taxpayers will be impacted equally.

Impact on the department and other agencies:  
The department will no longer be overburdened with evaluations and audits of the claiming of the exemption.

GENERAL FUND: Undetermined.

OTHER FUNDS: None.

PPBS PROGRAM DESIGNATION: None.

OTHER AFFECTED AGENCIES: None.

EFFECTIVE DATE: Taxable yeas beginning after December 31, 2013.